DOMINICAN REPUBLIC

The Department of State submitted this report to the Senate Committees on Foreign Relations and on Finance and to the House Committees on Foreign Affairs and on Ways and Means, on January 31, 1999.

Key Economic Indicators

(Billions of U.S. Dollars unless otherwise indicated)

	1996	1997	1998 1/
Income, Production and Employment:			
Nominal GDP 2/	13.5	15.0	16.2
Real GDP Growth (pct) 3/	7.3	8.2	7.0
GDP by Sector:			
Agriculture	1.6	1.9	2.1
Manufacturing	2.4	2.7	2.9
Services	3.7	4.7	5.2
Government	1.0	1.0	1.1
Per Capita GDP (US$)	1,572	1,882	2,000
Labor Force (000s)	3,522	3,614	3,697
Unemployment Rate (pct)	16.5	15.7	14.3
Money and Prices (annual percentage growth):			
Money Supply Growth (M2)	20	24	18
Consumer Price Inflation	4.0	8.3	9.0
Exchange Rate (DR Peso/US$ annual average)			
Official	12.90	14.01	14.71
Parallel	13.63	14.27	15.14
Balance of Payments and Trade:			
Total Exports FOB (US$ millions) 4/	4.1	4.8	4.8
Exports to U.S. 5/	3.6	4.4	4.4
Total Imports CIF (US$ millions) 4/	5.7	6.6	7.0
Imports from U.S. 5/	3.2	3.9	4.0
Trade Balance (US$ millions) 4/	-1.5	-1.8	-2.2
Trade Balance with U.S. 5/	0.4	0.5	0.4
External Public Debt	3.7	3.5	3.4
Fiscal Surplus/GDP (pct)	0.1	1.6	-1.7
Current Account Deficit/GDP (pct)	-1.8	-1.5	-1.0

Debt Service Payments/GDP (pct)	3.0	1.5	1.5
Gold and Foreign Exchange Reserves 6/	0.5	0.5	0.5
Aid from U.S. (US$ millions) 7/	13.3	11.6	13.3
Aid from All Other Sources	N/A	N/A	N/A

1/ 1998 figures are all estimates based on available monthly data through June.
2/ GDP at factor cost.
3/ Percentage changes calculated in local currency.
4/ Central Bank.
5/ U.S. Department of Commerce and U.S. Census Bureau; exports FAS, imports customs basis; 1998 figures are estimates based on data available through August.
6/ U.S. Embassy calculations of gross reserves including certain illiquid assets.
7/ Calculation based on U.S. fiscal year. 1998 figure does not include relief specifically related to Hurricane Georges.

Source: Economic Studies Department, Central Bank of the Dominican Republic, unless otherwise indicated.

1. General Policy Framework

The economy of the Dominican Republic continued its excellent rate of growth in the first three quarters of 1998, with the central bank predicting GDP growth of at least seven percent for the third year in a row. On September 22, Hurricane Georges hit the Dominican Republic causing extensive infrastructure and other damage. Early assessments put the damage in excess of $1 billion. Although it is still difficult at this time (November 1998) to evaluate the impact of the Hurricane on the overall economy, the central bank believes that GDP growth will be near seven percent and inflation will again be held to the single digit level. The official exchange rate was devalued nine percent from 14.02 to 15.33 pesos to the dollar in July 1998. It has continued to devalue slowly since then.

Because of the Dominican Republic's high propensity to import, changes in the exchange rate are politically significant. The need to keep the peso stable forces the central bank to maintain a high interest rate structure to retain short-term capital. Foreign exchange operations also play a role in meeting money supply targets since the central bank's purchase of pesos for dollars tends to reduce the money in circulation within the country.

According to the central bank, the money supply grew 18 percent from June 1997 to June 1998. The central bank regulates the money supply by issuance of new money through the banking system and by the purchase or issuance of debt instruments of the central bank itself. Since there is no secondary market for government securities and no liquid security market, the tools available to the central bank are limited. The central bank can modify bank reserve requirements but rarely does so. Banks resort to the discount window of the central bank only rarely. The Superintendency of Banks has continued its work to improve banking regulation. Although the Dominican Republic has no deposit insurance, the central bank guaranteed deposits at Bancomercio, the country's third largest bank, when it failed in early 1996, and subsequently supervised its sale to another Dominican bank. There have been no significant bank failures since then.

Gross foreign exchange reserves were approximately $521 million in June 1998. The reserve figures include some central bank assets, which are not actually available for use in payments. According to its latest report, the central bank calculates that its net liquid reserves are approximately $150 million. The government continued timely payments of foreign private bank debt and payments on renegotiated Paris Club debt. In late 1997, the Dominican Republic came to an agreement with the U.S. Department of Agriculture's Commodity Credit Corporation (CCC) for the payment of arrearages to that institution. In the aftermath of Hurricane Georges, however, the central bank has approached the Paris Club to request a six-month payment moratorium.

The government continues to compensate the central bank for foreign debt payments carried out on its behalf. In the past, the central bank obtained the dollars needed for debt service by monetary expansion and compensated for this expansion by issuing Certificados de Participacion, which are short-term debt instruments. While this helps absorb excess liquidity, interest payments on these certificates may also be covered by net money creation.

Prior to Hurricane Georges, government cash flows were in surplus according to the central bank. Relief and reconstruction expenditures will probably cause the government to run a minor deficit, but these expenditures may yet be offset by flows from the multilateral financial institutions. On an accrual basis, however, there is probably a significant deficit. The government has accumulated large arrears to domestic suppliers and contractors, although the Fernandez administration is moving slowly to repay some portion of this. The central government continues to provide subsidies to profligate state enterprises without regard to efficiency or production targets. The exact size of this debt is unknown, but has been variously put at the peso equivalent of 150 to 600 million dollars. This domestic debt is owed to foreign firms now or previously operating in the Dominican Republic, as well as to purely local firms. Current government financial flows leave substantial doubt about the ability of the Dominican Government to pay this debt. The government has considered covering this debt by the issuance of bonds.

The Dominican Republic has ratified the GATT 94 and participates in WTO meetings. The government has not yet fully implemented the Uruguay Round agreements, although it has taken important steps this year toward adopting the rectification agreement negotiated with the U.S. in 1996. Agricultural products continue to be imported based on a discretionary licensing system.

2. Exchange Rate Policy

The official exchange rate is set by the central bank. On July 2, 1998, the peso was devalued nine percent from 14.02 pesos/dollar to 15.33 pesos/dollar. It has continued to devalue slowly since then with the most recent official rate (November 1998) set at 15.46 pesos/dollar. The unofficial rate has also devalued and is currently in the range of 15.65-15.85 pesos to the dollar. Traditional exporters such as sugar, cocoa, and coffee producers, credit card companies, and airlines are still required by law to sell foreign exchange to the central bank at the official rate, but most businesses and individuals are free to carry out foreign exchange transactions through the commercial bank system. The market rate is influenced by central bank activities such as dollar sales and the use of its considerable regulatory discretion to "jawbone" banks.

3. Structural Policies

Most domestic prices are determined by market forces, although distortionary government policies sometimes limit the operation of these forces. High tariff and nontariff barriers also increase the cost of doing business in the Dominican Republic. Since tariff reform enacted by presidential decree in 1990 and modified by law in 1993, no further reform has affected U.S. exporters. In December 1996, President Fernandez submitted a proposal to Congress to decrease all tariffs. This proposal was not acted upon. Following the negotiation of a free trade pact with Central America, however, the Fernandez administration is expected to submit a new proposal to the Congress to decrease tariff levels to Central American levels (i.e. top tariff of 20 percent).

The 1990 tariff regime reduced and simplified the tariff schedule to six categories with seven tariff rates ranging from 3 to 35 percent. It also replaced some quantitative import restrictions with tariffs and transformed all tariffs to ad valorem rates. While it marked an improvement over the previous tariff regime, this reform still left the Dominican Republic with high trade barriers. Few imports actually enter at the maximum 35 percent tariff rate, however, since together with other taxes and fees, it acts as an effective barrier to trade. Since nearly 40 percent of government revenues come from duties, taxes and fees collected on imports, the government's flexibility in trade policy is limited.

The government has continued to implement changes in its tax system aimed at increasing revenues. The concept of taxable income has been enlarged, marginal tax rates on individuals and companies reduced and capital gains are no longer considered exempted income. The government is expected to submit proposals for changes in the tax system as part of a reform package in late 1998. In May 1992, a new labor code was promulgated with provisions which increased a variety of employee benefits. After an increase of 25 percent in 1997, public sector minimum wages have not increased in 1998.

Government policy prohibits new foreign investment in a number of areas including public utilities, national defense production, forest exploitation and domestic air, surface and water transportation. Government regulations, such as the process required to obtain the permits to open new businesses, choke economic growth and innovation. The difficulties of protecting intellectual property rights have slowed the use of modern medicines. Investment in modern agricultural techniques is impeded by a chaotic land tenure system, and the unwillingness of large landowners to modernize.

4. Debt Management Policies

The total external debt of the government is now approximately \$3.4 billion. A significant portion of the official debt was rescheduled under the terms of Paris Club negotiations concluded in November 1991. In August 1994, the government successfully concluded debt settlement negotiations with its commercial bank creditors. The deal involved a combination of buy-back schemes and U.S. Treasury-backed rescheduling. Payment to foreign private and public creditors in the financial sector has generally been current since then, particularly since the agreement noted above with the CCC.

Government payments to foreign non-financial institutions are notoriously slow. Some debts are ten years old. The Fernandez government continues to express its desire to resolve these debts, but progress has been limited.

5. Significant Barriers to U.S. Exports

Trade Barriers: Tariffs on most products fall within the 5 to 35 percent range. In addition, the government imposes a 5 to 80 percent selective consumption tax on "non-essential" imports such as home appliances, alcohol, perfumes, jewelry, and automobiles.

The Dominican Republic requires a consular invoice and "legalization" of documents, which must be performed by a Dominican Consulate in the U.S. Fees for this service vary by consulate but can be quite substantial. Some importers now pay the consular invoice fee in Santo Domingo directly to customs. Moreover, importers are frequently required to obtain licenses from the Dominican Customs Service.

There are food and drug testing and certification requirements, but these are not burdensome.

Customs Procedures: In the past, bringing goods through Dominican Customs was a slow and arduous process, but there is anecdotal evidence that this situation has improved. Customs Department interpretation of exonerated materials being brought into the country still provokes complaints, however, and businesspersons here sometimes spend considerable time and money to get items through customs.

Arbitrary customs clearance procedures sometimes cause problems for business. The use of "negotiated fee" practices to gain faster customs clearance continues to put some U.S. firms at a competitive disadvantage in the Dominican market. Customs officials routinely reject invoice prices as a basis for computing duties and customs fees and use their own assumed value database. This applies to virtually all non-free trade zone imports.

Government Procurement Practices: The Dominican Republic has a centralized Government Procurement Office, but the procurement activities of this office are basically limited to expendable supply items of the government's general office work. In practice, each public sector entity has its own procurement office, both for transactions in the domestic market and for imports. Provisions of the U.S. Foreign Corrupt Practices Act often put U.S. bidders on government contracts at a serious disadvantage in what are sometimes non-transparent bidding procedures.

Prohibitions on Land Ownership: A long-standing requirement that foreigners wishing to purchase land first obtain permission from the presidency was lifted in early 1998.

Investment Barriers: Legislation designed to improve the investment climate passed in November 1995. Its implementing regulations were issued by the Fernandez administration in September 1996. The legislation does not contain procedures for settling disputes arising from Dominican Government actions. The seizures of foreign investors' property by past governments which are still unresolved, refusal to honor customs exoneration commitments, and the government's slowness in resolving claims for payment reduce the attractiveness of the investment climate, notwithstanding passage of the 1995 legislation.

Foreign investment must receive approval from the Foreign Investment Directorate of the central bank to qualify for repatriation of profits (the new law provides for repatriation of 100 percent of profits and capital and nearly automatic approval of investments).

The electricity sector is a weak link in the Dominican economy. Businesses operating in the DR cannot depend on the public electric utility (CDE) to be a reliable source of electricity. Legislation governing the privatization/capitalization of CDE as well as of other state enterprises was passed by the Congress in June 1997. The capitalization of CDE is likely to occur in early 1999.

Foreign employees may not exceed 20 percent of a firm's work force. This is not applicable when foreign employees perform managerial or administration functions only.

Dominican expropriation standards (e.g., in the "public interest") do not appear to be consistent with international law standards; several investors have outstanding disputes concerning expropriated property. The Fernandez government continues to maintain that it wishes to resolve these issues although progress has been slow. The Dominican Republic does not recognize the general right of investors to binding international arbitration.

All mineral resources belong to the state, which controls all rights to explore or exploit them. Private investment has been permitted in selected sites. Currently, foreign investors are exploring for gold, natural gas, and copper. The process of choosing and contracting such areas has not been transparent.

Investors operating in the Dominican Republic's Free Trade Zones (FTZ's) experience far fewer problems in dealing with the government than do investors working outside the zones. For example, materials coming into or being shipped out of the zones are reported to move quickly, without the kinds of bureaucratic difficulties mentioned above.

6. Export Subsidies Policies

The Dominican Republic has two sets of legislation for export promotion: the Free Trade Zone Law (Law no. 8-90, passed in 1990) and the Export Incentive Law (Law no. 69, passed in 1979). The Free Trade Zone Law provides 100 percent exemption on all taxes, duties, and charges affecting the productive and trade operations at free trade zones. These incentives are provided to specific beneficiaries for up to 20 years, depending on the location of the zone. This legislation is managed jointly by the Foreign Trade Zone National Council and the Dominican Customs Service.

The Export Incentive Law provides for tax and duty free treatment of inputs from overseas that are to be processed and re-exported as final products. This legislation is managed by the Dominican Export Promotion Center and the Customs Service. In practice, use of the export incentive law to import raw materials for process and re-export is cumbersome and delays in clearing customs can take anywhere from 20-60 days. This customs clearance process has made completion of production contracts with specific deadlines difficult. As a result, non-free trade zone exporters rarely take advantage of the Export Incentive Law. Most prefer to import raw materials using the normal customs procedures which, although more costly, are more rapid and predictable.

There is no preferential financing for local exporters nor is there a government fund for export promotion.

7. Protection of U.S. Intellectual Property

The Dominican Republic belongs to the World Trade Organization (WTO), and is a signatory to the Paris Convention, Berne Convention, Madrid Agreement, and the Rome Convention. In 1998, the U.S. Trade Representative placed the Dominican Republic on the "Special 301" Priority Watch List because it continues to have inadequate enforcement of its existing laws and a legal regime that does not meet international standards. The government's actions to date to enforce the copyright law have not been sufficient to stem widespread piracy of video and audio tapes, compact discs, and software. While larger cable TV systems generally pay royalties to U.S. right holders, smaller ones continue to pirate satellite signals, and the government has not responded to requests from U.S. industry for more effective enforcement. Trademarks, particularly of apparel and athletic shoes, are commonly counterfeited and sold locally. The patent law still contains broad exceptions from patentability, and provides an inadequate term of protection.

Patents: Patents are difficult to receive and enforce against a determined intellectual property thief. In a local pharmaceutical market worth approximately $110 million per year, 70 percent of the total is locally produced or packaged. A significant percentage of that total is believed to be pirated. Resolutions issued by the government at year end 1996 and early 1997 further encourage the violation of pharmaceutical patents in the Dominican Republic. However, the Supreme Court recently upheld the rights of a foreign patent holder against a local laboratory.

Trademarks: Apparel and other trademarked products are counterfeited and sold in the local market. Although the Dominican Government is taking a more activist stance toward remedying shortcomings in this area, including seizure of pirated goods, protection remains problematic.

Copyright: Although copyright laws are generally adequate, enforcement is not, resulting in widespread piracy. Video and audio recordings and software are being counterfeited. Some television and cable operators are re-broadcasting signals without compensating either the original broadcaster or the originator of the recording. The Motion Picture Association of America (MPAA) estimates that losses in the Dominican Republic due to theft of satellite-carried programming are one million dollars per year.

Impact on U.S. Trade: Infringement of intellectual property rights is so widespread that quantifying its impact on U.S.-Dominican trade is virtually impossible.

8. Worker Rights

a. The Right of Association: The Constitution provides for the freedom to organize labor unions and also for the right of workers to strike (and for private sector employers to lock out workers). All workers, except military and police, are free to organize, and workers in all sectors exercise this right. The government respects association rights and places no obstacles to union registration, affiliation or the ability to engage in legal strikes. Organized labor represents little more than 10 percent of the work force and is divided among three major confederations, four minor confederations and a number of independent unions.

b. The Right to Organize and Bargain Collectively: Collective bargaining is lawful and may take place in firms in which a union has gained the support of an absolute majority of the workers. Only a minority of companies has collective bargaining pacts. The Labor Code stipulates that workers cannot be dismissed because of their trade union membership or activities.

The Labor Code applies in the 40 established Free Trade Zones (FTZs). The FTZ companies, over sixty percent of which are U.S.-owned or associated, employ approximately 172,000 workers, mostly women. Some FTZ companies have allegedly discharged workers who attempt to organize unions, but these allegations have primarily been made against non-U.S. companies.

c. Prohibition of Forced or Compulsory Labor: There were numerous reports of forced overtime in factories. Employers, particularly in the FTZs, sometimes locked the exit doors of factories after normal closing time so that workers could not leave. There have been reports of workers being fired for refusing to work overtime and both employers and workers state that new hires are not informed that overtime is optional.

d. Minimum Age for Employment of Children: The Labor Code prohibits employment of youth under 14 years of age and places restrictions on the employment of youth under the age of 16. These restrictions include a limitation of no more than six hours of daily work, no employment in dangerous occupations or establishments serving alcohol and limitations on nighttime work. Dominican law requires six years of formal education.

The high level of unemployment and lack of a social safety net create pressures on families to allow children to earn supplemental income. Tens of thousands of children work selling newspapers, shining shoes or cleaning cars, often during school hours. The government has proposed a fine for the parents of truant children.

e. Acceptable Conditions of Work: The Constitution provides the government with legal authority to set minimum wage levels and the Labor Code assigns this task to a National Salary Committee. Congress may also enact minimum wage legislation. The Labor Code establishes a standard work period of eight hours per day and 44 hours per week. The Code also stipulates that all workers are entitled to 36 hours of uninterrupted rest each week. The Code grants workers a 35 percent differential for work over 44 hours up to 68 hours per week and double time for any hours above 68 hours per week.

The Dominican Social Security Institute (IDSS) sets workplace safety and health conditions. The existing social security system does not apply to all workers and is underfunded.

Workplace regulations and their enforcement in the FTZs do not differ from those in the country at large, although working conditions are sometimes better. Conditions for agricultural workers are in general much worse, especially in the sugar industry.

f. Rights in Sectors with U.S. Investments: U.S.-based multinationals active in the FTZs represent one of the principal sources of U.S. investment in the Dominican Republic. Some companies in the FTZs adhere to significantly higher worker safety and health standards than do non-FTZ companies. In other categories of worker rights, conditions in sectors with U.S. investment do not differ significantly from conditions in sectors lacking U.S. investment.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad on an Historical Cost Basis **--** 1997

(Millions of U.S. Dollars)

Category		Amount
Petroleum		(1)
Total Manufacturing		321
Food & Kindred Products	21	
Chemicals & Allied Products	26	
Primary & Fabricated Metals	0	
Industrial Machinery and Equipment	0	
Electric & Electronic Equipment	0	
Transportation Equipment	0	
Other Manufacturing	274	
Wholesale Trade		19
Banking		34
Finance/Insurance/Real Estate		(2)
Services		20
Other Industries		(1)
TOTAL ALL INDUSTRIES		476

(1) Suppressed to avoid disclosing data of individual companies.
(2) Less than $500,000 (+/-).

Source: U.S. Department of Commerce, Bureau of Economic Analysis.